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Supreme Court, U.S.
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No. 04-1208

IN THE

Supreme Court of the United States

ANN MOSTOLLER, TRUSTEE,

Petitioner,

v.

CWCAPITAL LLC,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether this Court should revisit the Court of Appeal's unanimous decision affirming the summary judgment dismissal of a Bankruptcy Trustee's breach of contract claims in which the Trustee sought to preclude a government-approved mortgage lender from enforcing the terms of a mortgage loan insured under the National Housing Act based upon a purported unwritten modification of the loan documents where:

a) there is no conflict among the Circuits regarding the fact that loans insured by the Secretary of the Department of Housing and Urban Development under the National Housing Act cannot be modified orally or through theories of estoppel or waiver; and

b) the Court of Appeals specifically considered state law as well as federal law and determined that such a mortgage loan cannot be modified orally or through theories of estoppel or waiver under either federal or state law.

PARTIES TO THE PROCEEDING

Ann Mostoller, Trustee is the bankruptcy trustee (the "Trustee") with respect to the estate of West Pointe Properties, LP ("West Pointe"). CWCapital LLC ("CW") is a mortgage lender approved by the United States Department of Housing and Urban Development ("HUD") to originate and service loans insured by and administered through HUD. CW is not owned or controlled by any publicly traded corporation. HUD was a co-defendant in this action before the District Court. However, the Trustee sought only to appeal the grant of summary judgment to the Sixth Circuit with respect to CW, not HUD. CW, as mortgage lender, noticed the borrower's default at the request of HUD and subsequently assigned the loan to HUD at HUD's direction. HUD, not CW, ultimately foreclosed upon the mortgaged property.

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STATUTORY PROVISIONS INVOLVED

This matter involves a dispute over the enforcement of the terms of a mortgage loan federally insured by the United States Department of Housing and Urban Development pursuant to the National Housing Act, 12 U.S.C. § 1701 *et seq.* (2001). In particular, section 1715z-4 governs the modification of mortgage documents covering multifamily housing. It states in pertinent part that:

> The Secretary shall not consent to any request for curing a default under any mortgage covering multifamily housing . . . or for a modification of the terms of such mortgage, except in conformity with regulations prescribed by the Secretary in accordance with the provisions of this section.

12 U.S.C. § 1715z-4 (2001).

STATEMENT OF THE CASE

The Trustee sets forth an extensive factual recitation in her Petition for Writ of Certiorari (the "Petition") based upon her contention that there "was reliance on factual errors by the lower courts in their opinions." [Petition at 3]. While the Court rarely grants certiorari "when the asserted error consists of erroneous factual findings," U.S. Sup. Ct. R. 10, and since the Trustee's recitation of the "facts" is not supported by the record below, CW will provide the facts as resolved by the lower courts which are amply reflected in the record below.

HUD has various programs through which it promotes the creation of affordable housing by facilitating the construction or substantial rehabilitation of multifamily housing communities such as apartments and manufactured home parks. National Housing Act ("NHA"), 12 U.S.C.

§ 1701 *et seq.* (2001). It does so by, among other things, insuring HUD-approved lenders against loss on mortgage defaults. *Id.* One such program, commonly known as the Section 207 Program, encourages the construction or rehabilitation of manufactured home parks through such HUD-insured loans. 12 U.S.C. § 1713 (2001) (the "Section 207 Program"). Although HUD is not the original lender on loans made under the Section 207 Program, HUD bears the economic risk of loss should a borrower default on its loan. Because the ultimate risk of these loans is borne by the government, HUD-approved lenders (i.e. lenders approved and licensed by HUD to enter into loan agreements with respect to such loans) must strictly comply with rigid statutory, regulatory and contractual obligations in connection with the handling of these loans.

If a default (monetary or non-monetary) occurs under a mortgage loan insured by HUD under the Section 207 Program, the lender is obligated to (i) assign the defaulted loan to HUD in exchange for mortgage insurance benefits or (ii) foreclose upon (or otherwise acquire title to) the mortgaged property and convey it to HUD in exchange for mortgage insurance benefits. 24 C.F.R. § 207.258 (2004). The lender's economic risk of loss is limited to an assignment fee equal to 1.0% of the outstanding loan amount (if the lender elects to assign the defaulted loan to HUD) and the loss of one month's interest on the loan. HUD's regulations, rules and requirements, therefore, give HUD broad controls and authority with respect to the underwriting and administration of loans insured by it. 24 C.F.R. § 200 *et seq.* (2004). In fact, HUD has the sole final discretion on such loans with respect to the terms of the loan agreements, any modifications of the loan documents, any extensions of any deadlines imposed under the loan documents, any advances of monies under the loan documents and any changes to the building plans and specifications. *Id.* The HUD-approved lender must comply with any determinations of HUD.

In 1996, West Pointe obtained a HUD-insured loan through Continental Wingate Associates, Inc., CW's predecessor, in the amount of $2,222,900.00 pursuant to the Section 207 Program, for the purposes of developing and constructing a mobile home park to be known as the West Pointe Community Mobile Home Park (the "Project"), in Knoxville, Tennessee (the "HUD-Insured Loan"). Petitioner's Appendix ("Pet'r App.") at A-16.[1] In connection with the HUD-Insured Loan, West Pointe executed a Deed Of Trust Note ("Note"), a Deed of Trust ("Deed of Trust"), a Security Agreement ("Security Agreement"), a Building Loan Agreement ("Building Loan Agreement"), a Regulatory Agreement ("Regulatory Agreement") and various other HUD-form documents required by HUD as a condition of insuring the HUD-Insured Loan (collectively, the "Loan Documents").[2] *Id.* Through the Loan Documents, CW, after

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[1] The District Court opinion below in *Mostoller v. HUD*, No. 3:02-CV-291 (E.D. Tenn. Jul. 18, 2003) granting CW and HUD's motions for summary judgment and dismissing the action is reproduced in the Petitioner's Appendix at A-15 through A-31.

[2] Another document executed by West Pointe at the closing of the HUD-insured Loan was a Remarketing and Extension Agreement which the Trustee disingenuously characterizes as an "Extension Agreement." [Petition at 6-7]. Before the Sixth Circuit, the Trustee claimed for the first time (as it misleads this Court in the Petition) that the Remarketing and Extension Agreement "sets forth the terms of continued construction" if "CW elects not to terminate the loan." [*Id.*]. However, as correctly emphasized by the Sixth Circuit, this agreement

> specifically **disclaims** any modifications of the deadline or any other requirement in the loan agreement: [by stating] . . . Lender's right to receive fees for extending the date of Final Endorsement shall not be construed to give [West Pointe] the right to any extension . . . [West Pointe] acknowledges that [CW] is not

(Cont'd)

permission and authorization from HUD, agreed to make advances of loan proceeds to West Pointe to fund the construction of the Project. *Id.* The Note obligated West Pointe to repay the HUD-Insured Loan pursuant to a fixed schedule with interest only due for the first eleven months and principal and interest due each month thereafter. *Id.* The Note was secured by the Deed of Trust, which placed a first lien on the Project and provided various remedies in the event of a default. The Deed of Trust provided that a default under either the Building Loan Agreement or the Regulatory Agreement constituted a default under the Deed of Trust. *Id.*

Pursuant to the Building Loan Agreement, West Pointe was required to complete construction of the Project by July 7, 1997, eleven months after the closing of the HUD-Insured Loan. *Id.* at A-17. The Construction Contract that West Pointe signed with its general contractor, J. Hicks Excavating, Inc., however, provided for a shorter construction period to ensure that West Pointe's obligations under the Loan Documents could be fulfilled. *Id.* Both the Building Loan Agreement and the Construction Contract provided that any changes therein had to be approved in writing by CW and HUD. *Id.* In addition, the Construction Contract provided that "[t]he time by which the work shall be completed may be extended in accordance with the terms of said AIA General Conditions only with the prior written approval of the Commissioner [HUD]." *Id.* West Pointe acknowledged in the Building Loan Agreement that failure to complete the Project by July 7, 1997 or cessation of work on the Project for a period of more than 20 days (among other things) constituted defaults. *Id.* In addition, the Deed of Trust and the Security Agreement,

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(Cont'd)

> obligated to grant any extensions . . . and that by granting of one or more extensions shall not obligate [CW] to grant any additional or further extensions.

Pet'r App. at A-10-11 (emphasis supplied).

through which West Pointe pledged the Project and certain other property as collateral for the HUD-Insured Loan, specifies various events of default including failure to make a payment when due and a default or breach of any of the Loan Documents. *Id.*

Upon an event of default, CW was authorized to accelerate the HUD-Insured Loan and declare a default. *Id.* The Security Agreement signed by West Pointe and CW provided that "no waiver by the Secured Party [CW] of any event of default [would] operate as a waiver of any other event of default or of the same event of default on a future occasion." *Id.* Moreover, CW, as the secured party, could "delay in exercising or omit to exercise any right or remedy . . . without waiving that or any past, present or future right or remedy." *Id.* at A-17-18. The Security Agreement also contained a prohibition against unwritten modifications in that it stated it "may not be amended, altered or changed other than in a writing signed by" CW and West Pointe and the Security Agreement and the other "Loan Documents represent the entire agreement between [CW] and [West Pointe]."[3] *Id.* Finally, at closing, West Pointe executed a Certification of Mortgagor that certified that "the terms and conditions of the loan as reflected in the Loan Documents have not been amended, modified or supplemented, directly or indirectly, by any other agreement or understanding of the parties or waiver of any of the material provisions of the Loan Documents." *Id.*

From almost the outset of the construction of the Project, problems arose with the progress of construction. *Id.* Under

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[3] Not only did the Loan Documents and HUD regulations require that all modifications be in writing, but the HUD Form 92437 entitled Request for Construction Changes on Project Mortgages (which West Pointe routinely utilized during the construction of the Project) specified that "time extension[s must be] on a separate form."

the Loan Documents, as between CW and HUD, the responsibility for inspecting the progress of completion and conformity of the construction work was vested entirely with HUD. *Id.* HUD inspection reports from an early date reflected slow and problematic construction. *Id.* In January 1997, West Pointe submitted a request for a six-month extension of the construction completion date. HUD denied in writing the request for the six-month extension and permitted only an additional 87 days for rain delays, extending the date from February 1997 until May 1997. *Id.* West Pointe failed to complete the construction within the time allotted. *Id.* On May 8, 1997, West Pointe submitted a second extension request, which was rejected by HUD in writing on July 9, 1997. *Id.* In a letter dated July 9, 1997, HUD's representative, William McClister, explained the reason for the denial of the request to extend the construction completion deadline as "unacceptable" because: "[a]dditional time to complete the work has not been justified as required by the general conditions. Also, my staff has not observed a proper, concerted effort . . . to complete this job in a timely manner." *Id.* No extension could be given without HUD's approval. *Id.*

As of July 7, 1997 – with construction only about twenty percent completed – West Pointe was in default under the Loan Documents for its failure to complete construction by the construction completion deadline set forth in the Loan Documents. The Loan Documents explicitly required written approval by HUD for the construction completion deadline to be extended. *Id.* at A-10;[4] *see also* Pet'r App. at A-17-18. It is undisputed that no such approval was granted. To make matters worse, the general contractor ceased construction and withdrew his equipment and personnel from the job in July

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[4] The Sixth Circuit's opinion in *Mostoller v. CWCapital, LLC*, 2004 FED App. 0148N (6th Cir.) is reproduced in the Petitioner's Appendix at A-1 through A-12.

and then again, permanently, in October 1997 following disputes with West Pointe. *Id.* at A-19. In December 1997, approximately ten months after the original construction completion deadline of February 1997, and seven months after the extended construction completion deadline approved by HUD, the Project was still only twenty-five to thirty percent completed and there was no hope that construction could be completed in less than another year. Indeed, West Pointe could not obtain another general contractor at that time. *Id.* at A-4, A-19.

In addition to the construction-related defaults under the Loan Documents, West Pointe failed to make payments due under the Loan Documents. *Id.* at A-5. First, West Pointe failed to pay $23,566 to keep the HUD-Insured Loan in balance pursuant to the approval of a change order requested by West Pointe and approved by HUD which was conditioned upon funding of it by West Pointe.[5] *Id.* In addition, West Pointe breached the terms of the Loan Documents by failing to make the payment of interest and escrows due on November 1, 1997. *Id.*

On November 5, 1997, HUD notified CW in writing that West Pointe "may have violated various provisions of the [Building Loan Agreement]" and directed CW's attention to the "remedies available to the lender in the case of a default by the borrower." *Id.* at A-19. In that letter, HUD listed a litany of potential improper actions taken by West Pointe including concerns that the borrower was also impermissibly functioning as the general contractor, that Mr. Ronald Frye (West Pointe's former principal) had improperly removed the general contractor from the Project, that the borrower

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[5] Failure to keep the HUD-Insured Loan in balance (i.e. to provide funds in excess of unadvanced loan proceeds needed to complete the Project) constituted another default under the Building Loan Agreement.

apparently had failed to deposit the amount of $23,566 as required by a fourth Change Order and that HUD procedures precluded additional advances when this occurs. *Id.* at A-5. HUD made it clear to CW that no further advances of loan proceeds would be approved and that CW had to declare a default and assign the HUD-Insured Loan to HUD or exercise one of its other options for defaulted loans or lose the right to its mortgage insurance benefits. *Id.* at A-19.

As a result of the monetary and other numerous defaults under the Loan Documents, on December 10, 1997, acting upon HUD's recommendation, CW declared the HUD-Insured Loan in default and exercised its right pursuant to the Loan Documents to accelerate the HUD-Insured Loan. *Id.* Indeed, CW did not have any discretion with respect to the decision to declare the default as CW was required, pursuant to HUD regulations, to declare the default at that time.[6] Thereafter, CW assigned the HUD-Insured Loan to HUD in accordance with HUD regulations.[7] *Id.*

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[6] HUD regulations clearly define what constitutes a default. 24 C.F.R. § 207.255. Defaults are defined as "failure of the mortgagor to make **any** payment due under the mortgage" and "failure to perform **any** of the covenants under the provisions of the mortgage." 24 C.F.R. § 207.255(a)(1-2) (emphasis supplied). CW was required to notify the Commissioner in writing of such default "within 30 days." 24 C.F.R. § 207.256(a). An uncured default, which continues for a period of 30 days, triggers a mortgagee's entitlement to insurance benefits. 24 C.F.R. § 207.255(c). A mortgagee's failure to provide the notice of default within the required time limitations could result in a loss of the insurance benefits under the Section 207 Program.

[7] CW had sought permission from HUD for an extension of time to assign the HUD-Insured Loan; but **HUD denied** that request. It was within HUD's sole discretion whether to permit additional time for the election to assign. 24 C.F.R. § 207.258(b). Thereafter, CW did not have discretion as to how to handle the defaulted HUD-Insured Loan. It was required either to assign the HUD-Insured Loan to HUD or to acquire and convey title to the Project through foreclosure or other proceedings. 24 C.F.R. § 207.258.

After CW assigned the HUD-Insured Loan to HUD, all rights and duties of CW with respect to the HUD-Insured Loan were transferred from CW to HUD. *Id.* CW received no economic or other benefit from the declaration of default and the assignment.[8] Thereafter, while CW was no longer involved in any manner with the HUD-Insured Loan or the Project, West Pointe had an additional year an a half to cure the defaults or reach a work-out agreement with HUD in order to prevent foreclosure. *Id.* at A-5-6, A-19-20. HUD notified West Pointe on February 18, 1997 that CW had assigned the mortgage and invited West Pointe to cure the default. *Id.* at A-19. Over a month later, HUD notified West Pointe that the funds necessary to avoid foreclosure had not been received and provided West Pointe with an opportunity to show reasons why foreclosure should not take place. *Id.*

In response, West Pointe submitted an extensive memorandum to HUD in which it blamed HUD for the default and for CW's declaration of that default, stating that HUD directed CW to declare the loan in default, accelerate the balance and assign the Loan to HUD by virtue of its letter to CW dated November 5, 1997. Despite West Pointe's contentions that HUD (not CW) acted improperly in declaring the default, West Pointe had ample opportunity not only to cure the default, but also to establish, through the administrative proceedings conducted on May 14, 1998 afforded West Pointe by HUD, that the default did not exist or that foreclosure should not go through for some other reason. *Id.* at A-20. However, West Pointe failed to prove either. Rather, after a full hearing on these issues, apparently unconvinced, on November 9, 1998, HUD notified West

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[8] Rather, pursuant to HUD regulations, CW incurred a loss as it received insurance benefits that amounted to less than the full amount of the outstanding principal balance on the HUD-Insured Loan and HUD became the lender of record under the Loan Documents to pursue either a work-out with West Pointe or foreclosure.

Pointe that, pursuant to its discretion, the agency had considered all of the materials and allegations advanced by West Pointe regarding not proceeding with foreclosure and had concluded that West Pointe had "presented no legal reasons to alter HUD's decision to foreclose." *Id.* HUD held the HUD-Insured Loan for nearly a year and a half before publishing a foreclosure notice with the sale scheduled for May 27, 1999. *Id.*

West Pointe filed bankruptcy in order to stay the foreclosure by HUD. *Id.* The bankruptcy court granted HUD's motion for relief from the automatic stay and permitted HUD to foreclose on the Project. *Id.* In granting relief from the stay, the bankruptcy court stated that it was "undisputed that the Debtor (West Pointe) had made no principal payments on the August 7, 1996 Deed of Trust Note since its inception; that the Debtor had no income; . . . and that the Debtor last performed work on the property in late October 1997." *Id.* On April 27, 2000, HUD foreclosed on West Pointe's mortgage. HUD sold the Project to the highest bidder at a price of $350,000. *Id.*

The Complaint against CW and HUD was brought by West Pointe as debtor in possession[9] and asserted claims for damages under a breach of contract claim as a result of the foreclosure by HUD. *Id.* Originally, West Pointe asserted that CW should not have declared the HUD-Insured Loan in default, contending that the Building Loan Agreement was modified by oral representations providing for an "indefinite" extension of the construction deadline. *Id.* In the alternative, West Pointe asserted that a letter from HUD dated July 9, 1997 extended the completion date for the Project and that CW and HUD breached that agreement by foreclosing. *Id.*

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[9] The bankruptcy action was later converted to Chapter 7 and the Trustee continued this case under her name on behalf of West Pointe's estate.

After the lower court granted summary judgment to both CW and HUD, the Trustee appealed as to CW only, abandoning her claims that the July 9th letter extended the completion date and abandoning her argument that there was an oral modification of the loan documents. *Id.* at A-9 n.2. Instead, the Trustee claimed that CW was barred from enforcing the terms of the Loan Documents by virtue of theories of estoppel and waiver. The Trustee abandoned her claims against the government recognizing that these theories cannot be invoked against the government. *Id.* at A-8 n.1. Yet, she pursues these theories against CW – a HUD-approved lender acting at HUD's direction – for damages purportedly caused by HUD's foreclosure of the Project.

THE DECISIONS BELOW

Before the District Court, the Trustee argued that CW should not have declared a default because the Loan Documents were modified and the construction completion deadline was extended by oral representations (Pet'r App. at A-24) or by the July 9, 1997 letter. *Id.* at A-26. The District Court fully and carefully considered the full record and concluded that West Pointe was in default and that CW properly declared the loan in default and assigned the loan to HUD. *Id.* at A-29. The District Court held that the Loan Documents could not be modified by an oral representation, but rather that any modifications had to be in writing and approved by the Commissioner of HUD. *Id.* at A-24. The District Court also held that the July 9, 1997 letter was not an amendment to the Loan Documents because it was not a valid modification. *Id.* at A-28. Finally, the District Court held that CW never waived its right to declare a default. *Id.* at A-29.

On appeal to the Sixth Circuit, the Trustee abandoned her theory that the Loan Documents were orally modified and instead argued that CW somehow forfeited its rights to

declare the loan in default, relying on theories of estoppel or waiver. *Id.* at A-8-9. The Sixth Circuit unanimously rejected the Trustee's arguments, holding that "common law doctrines of waiver and estoppel cannot modify the terms of a HUD-guaranteed loan," and noting that this result would be the same under Tennessee common law. *Id.* at A-11. Indeed, the Sixth Circuit found that West Pointe was unable to establish that the July 9, 1997 letter or any conduct of CW could form the basis of a waiver or estoppel claim. *Id.* at A-11-12. The Sixth Circuit stressed that the plain terms of the Loan Documents applied and that CW was fully within its rights to declare West Pointe in default. *Id.* at A-12.

REASONS FOR DENYING THE PETITION

A. Standard of Review.

Generally, the Court "will decline to consider questions presented in a petition for certiorari that have not been considered by the lower court." *Patrick v. Burget*, 486 U.S. 94, 99 n.5 (1988); *see also, e.g., Nat'l Collegiate Athletic Ass'n v. Smith*, 525 U.S. 459, 470 (1999) ("[W]e do not decide in the first instance issues not decided below."); *J. Truett Payne Co. v. Chrysler Motor Corp.*, 451 U.S. 557, 568 (1981) ("We do not ordinarily address for the first time in this Court an issue which the Court of Appeals has not addressed.").

In addition, the Court generally only grants certiorari "for compelling reasons," where either there is a circuit split on the issue or where there is an important federal question at issue. U.S. Sup. Ct. R. 10; *see, e.g. Bunting v. Mellen*, 124 S. Ct. 1750, 1752 (2004) ("The second reason justifying a denial of certiorari is the absence of a direct conflict among the Circuits."); *Comm'r v. Estate of Bosch*, 387 U.S. 456, 457 (1967) (granting certiorari to resolve a "widespread

conflict" among the Circuits); *Rice v. Sioux City Mem'l Park Cemetery*, 349 U.S. 70, 79 (1955) (stating the importance of consistency in not granting certiorari "except in cases involving principles the settlement of which is of importance to the public, as distinguished from that of the parties, and in cases where there is a real and embarrassing conflict of opinion and authority between the Circuit Courts of Appeals"). Finally, the Court rarely grants certiorari "when the asserted error consists of erroneous factual findings or the misapplication of a properly stated rule of law." U.S. Sup. Ct. R. 10.

In this case, the Petition presents questions that were not raised or considered in any of the courts below. None of the questions presented involve a split in the Circuits or an important federal question. Finally, the Petition bases its request for certiorari on purportedly erroneous factual findings in the court below. For these reasons, the Petition should be denied and certiorari should not be granted.

B. Federal Law Governs This Dispute by Virtue of HUD's Participation as Loan Insurer and There is No Split in the Circuits to the Contrary.

The Trustee's basic contention in this litigation is that the terms of the Loan Documents governing the debtor's HUD-Insured Loan could not be enforced based upon various vague "equitable-type" claims. The Trustee apparently concedes that these equitable-type remedies are unavailable under federal law but disputes the applicability of federal law to the HUD-Insured Loan based upon her decision to pursue her appeals against the private HUD-approved lender alone.

The National Housing Act, 12 U.S.C. § 1715z-4, governs the requirements for the cure of defaults under, and the modification of, mortgage documents covering multifamily housing. It states in pertinent part that:

> The Secretary shall not consent to any request for curing a default under any mortgage covering multifamily housing . . . or for a modification of the terms of such mortgage, except in conformity with regulations prescribed by the Secretary in accordance with the provisions of this section.

12 U.S.C. § 1715z-4.

Indeed, every Circuit interpreting purported modifications to HUD-insured loans has held that federal law governs the interpretation of a HUD-insured loan and the rights and liabilities of the parties under such a loan. *VS Ltd. P'Ship v. HUD*, 235 F.3d 1109, 1113 (8th Cir. 2000) (specifically applying federal law – the National Housing Act and HUD regulations – in concluding that HUD loan documents can only be modified by a signed writing); *United States v. Victory Highway Vill., Inc.*, 662 F.2d 488, 497 (8th Cir. 1981) ("federal law, not [state] law, governs the rights and liabilities available upon default of a federally held or insured loan"); *United States v. Scholnick*, 505 F.2d 160, 164 (6th Cir. 1979) ("an overriding federal interest in protecting the funds of the United States and in securing the federal investments predominates over state interests."); *United States v. View Crest Garden Apts.*, 268 F.2d 380, 383 (9th Cir.) ("Local rules limiting the effectiveness of the remedies available to the United States for breach of a federal duty can not be adopted."), *cert. denied* 361 U.S. 884 (1959); *see also Bayvue Apts. Joint Venture v. Ocwen Fed. Bank FSB*, 971 F. Supp. 129, 131 (D.D.C. 1997) (district court applying federal law); *Teitelbaum v. HUD*, 953 F. Supp. 326, 331 (D. Nev. 1996) (district court applying federal law).

The Trustee argues, relying upon three unrelated cases not raised in her briefs below, *United States v. Kimbell Foods, Inc.*, 440 U.S. 715 (1979),[10] *Parker v. USDA*, 879 F.2d 1362 (6th Cir. 1989)[11] and *Pankow Constr. Co. v. Advance Mortgage Corp.*, 618 F.2d 611 (9th Cir. 1980),[12] that even if

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[10] In *Kimbell Foods*, the Court considered whether a uniform federal rule was needed to determine the priority of Farmers Home Administration and Small Business Association liens (pursuant to their respective loan programs) with respect to private liens. The Court held that there were intricate, well-established state laws of general applicability which obviated the need to fashion a uniform federal rule. Unlike the situation presented in *Kimbell*, in this case a clear federal rule barring unwritten modifications to HUD-insured loan documents and a clear federal regulatory scheme – embodied at 24 C.F.R. § 207.256b and 24 C.F.R. § 221.761(a)(2) – already exist under which to resolve the dispute at issue in the present action. Furthermore, the ruling in *Kimbell Foods* spoke to the regulation of private and consensual lien priorities and is neither dispositive nor reflective in any way of the transaction at issue in the present action.

[11] The Trustee inappropriately seeks to extend the dicta of *Parker* from the context of the Farmers Home Administration ("FmHA") loan program to HUD's Section 207 insured loan program. Such a leap is misguided, as the guidelines of the FmHA program are markedly distinct and, indeed, less stringent, than those of the HUD Section 207 loan program. Indeed, the dicta from *Parker* regarding the relationship between the FmHA, the lender and the borrower has little, if anything to do with the relationship between HUD, CW and West Pointe and even less to do with the application, in this case, of federal law. The *Parker* case does not even address the issue of the applicability of federal law. Moreover, it is clear that the *Parker* case does not support the argument that there is a conflict among the Circuits with respect to the issues raised in this case since *Parker* (like the decision below) is a Sixth Circuit case.

[12] The Trustee erroneously seeks to analogize the issue at bar to *Pankow*, in which the court found the application of California state law appropriate in resolving a dispute between a general

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federal law prohibits the enforcement of non-written modifications of loans against the government, this is not the case with respect to private lenders. However, no such distinction exists. These three cases do not support the Trustee's analysis of the specific type of HUD-sponsored lending relationship at issue here. Indeed, these cases are factually very different and their legal holdings do not support the Trustee's contentions. In fact, since HUD steps into the shoes of the HUD-insured lender when a defaulted HUD-insured loan is assigned to HUD, it would be prejudicial to the government to allow a private lender to waive rights under the loan documents without HUD's approval or to estop the government from enforcing the loan documents.

Moreover, cases with similar facts have all concluded that the prohibition against non-written modifications to HUD-insured loans applies with equal force whether the government or a private lender is involved. *Bayvue Apts. Joint Venture v. Ocwen Fed. Bank FSB*, 971 F. Supp. 129, 131 (D.D.C. 1997) (in stating that "since [private bank] was never a party to the alleged *de facto* modification agreement, the question of redressability turns on whether the alleged *de facto* agreement is or ever was enforceable," the court did

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contractor and a mortgage borrower who had secured funding under the National Housing Act. The dispute involved a private construction contract, rather than a loan document governed by HUD regulations and neither HUD nor the lender was a party to the dispute. In light of the fact that the present dispute is between the borrower and HUD-approved lender, and is wholly governed by federal regulations – any inference made by the Trustee that the holding in *Pankow* is applicable to the present action is wholly inappropriate. Additionally, the Trustee, in seeking to establish state law as the governing standard for the present action, completely ignores the Sixth Circuit's finding that "West Pointe's waiver and estoppel claims are baseless even if we apply Tennessee common law." Pet'r App. at A-11. The Ninth Circuit's ruling in *Pankow* is in no way "on point" with the current dispute and is certainly not dispositive of the issue in this case.

not distinguish between enforceability of the loan modification against the private lender or the government); *Multifamily Mortgage Trust 1996-1 v. Century Oaks Ltd.*, 532 S.E.2d 578, 582 (N.C. Ct. App. 2000) (upholding summary judgment for lender on borrower's claims that terms of loan documents were waived by a provisional work out agreement); *see also Victory Highway Vill., Inc.*, 662 F.2d at 497 (in stating that "federal law, not [state] law, governs the rights and liabilities available upon default of a federally held or insured loan," the court made no distinction between whether enforcement was against the government or the private lender).

The court in *Victory Highway* emphasized the importance of the enforcement of the terms of federally insured mortgages explaining:

> It is essential to the confidence of public and private lenders that the clear written terms of mortgages be implemented and enforced by the courts. Without such enforcement, **extrinsic judicial doctrines that frustrate the terms of the mortgage documents, and any subsequent 'work-out' arrangements, will impair the confidence of public and private lenders.** Through strict enforcement of the terms of the mortgages and recognition of HUD's right to foreclose on default, "the federal policy to protect the treasury and to promote the security of federal investment which in turn promotes the prime purpose of the Act to facilitate the building of homes by the use of federal credit will be preserved."

Victory Highway, 662 F.2d at 495 (emphasis supplied). The court explicitly rejected any type of waiver or estoppel argument which contradicted the terms of the written loan documents despite a written provisional month-to-month

work out arrangement. Indeed, the court made clear that the delay in exercising the right to pursue foreclosure does not indicate a waiver of the right to foreclose nor does it constitute an indefinite extension of the borrower's right to cure a default as advocated by the Trustee here. Once again, the application of such theories as waiver or estoppel to CW would have the effect of a waiver or estoppel of HUD's rights as CW's assignee of the loan. In such instances, the government, not CW, would incur the loss.

Not only is the Trustee's theory of recovery barred by the law, but there is nothing in the record to support such a waiver claim. Indeed, as indicated by the trial court, the undisputed facts indicate that CW did not have the authority and discretion to "waive" any rights under the Loan Documents, did not relinquish the right to declare the HUD-Insured Loan in default and made no indications to the contrary. Pet'r App. at A-28-29. The Trustee concedes that there has been no written expression of waiver. The Trustee does not assert any consideration for her waiver theory. And, at the time when CW (at the recommendation of HUD) declared the HUD-Insured Loan in default and assigned it to HUD, there was no possibility of West Pointe curing the defaults in the near future. To judicially create an indefinite extension of the construction completion deadline imposed by the Loan Documents with respect to the HUD-Insured Loan would frustrate the heart of the prohibitions against unwritten modifications and create a fraud upon the federal purse.[13] Since the waiver and estoppel theories are inapplicable to federally-insured interests and the Loan Documents cannot be modified by waiver or any other theory absent a writing expressing such modification, the trial court's

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[13] Under the Trustee's theories, a lender would have to declare a default and move to enforce its remedies immediately upon the occurrence of a default or lose forever its ability to enforce its rights. *See* Pet'r App. at A-11-12.

decision granting summary judgment and the Sixth Circuit's decision affirming the summary judgment dismissal were proper. Indeed, there is no split among the Circuits on this issue. The Sixth Circuit ruled in precisely the same manner as each of the other Circuits considering this issue.

C. The Equitable Remedies Claimed Are Unavailable and Do Not Rise to the Level of an Important Federal Issue.

As correctly concluded by the Sixth Circuit and the District Court below, the Trustee's claims that the terms of the HUD-Insured Loan Documents were modified through estoppel, waiver or some other theory is unsupported by federal law. Indeed, the various Circuits all hold that federal law precludes the modification of the Loan Documents in any manner other than through a written modification signed by all of the parties.

The National Housing Act prohibits modification of mortgage agreements through oral agreements, estoppel, waiver or other extrinsic judicial remedies. *VS Ltd. P'Ship v. HUD*, 235 F.3d 1109, 1113 (8th Cir. 2000); *Bayvue Apts. Joint Venture v. Ocwen Fed. Bank FSB*, 971 F. Supp. 129, 131 (D.D.C. 1997); *Teitelbaum v. HUD*, 953 F. Supp. 326, 331 (D. Nev. 1996). And, the applicable HUD regulations require all modifications of a mortgage agreement be made only when the parties reach such terms in writing and only with the approval of the Commissioner of HUD. 24 C.F.R. § 207.256b; *see* 24 C.F.R. § 221.761(a)(2).

For example, 24 C.F.R. § 207.256b states, in relevant part,

> The mortgagor and the mortgagee may, **with the approval of the Commissioner**, enter into an agreement which extends the time for curing a default under the mortgage or modifies the payment terms of the mortgage. The Commissioner's approval of [this] type of agreement . . . shall not be

> given unless the mortgagor agrees **in writing** that . . . it will hold in trust for disposition as directed by the Commissioner all rents or other funds derived from the property which are not required to meet actual and necessary expenses arising in connection with the operation of such property, including amortization charges under the mortgage.

(emphasis supplied). Similarly, 24 C.F.R. § 221.761(a)(2) states, in relevant part:

> In a case where the mortgage is in default, the mortgagor and the mortgagee may enter into a forbearance agreement . . . if . . . [t]he Commissioner determines that the default was due to circumstances beyond the mortgagor's control and that the mortgage probably will be restored to good standing within a reasonable period of time **and evidences such determination by written approval of the forbearance agreement**.

(emphasis supplied).

The Trustee misleadingly relies on several cases never referenced below for her theory that extrinsic judicial doctrines such as estoppel and waiver are applicable here. The Trustee's citation of *Heckler v. Cmty. Health Servs. of Crawford County, Inc.*, 467 U.S. 51 (1984) for the proposition, stated in dicta, that estoppel may lie against the government under certain circumstances is a red herring.[14]

[14] The Trustee also cites *Unites States v. Fox Lake State Bank*, 366 F.2d 962 (7th Cir. 1966), *Resolution Trust Corp. v. Vanderweele*, 833 F.Supp. 1383 (N.D. Ind. 1993) and *In re Lane*, 96 B.R. 164 (Bankr. C.D. Ill. 1988) for this proposition. These cases are inapposite. The *Fox Lake* court, ruling in a case where the government was bringing suit against a bank under the Civil False Claims Act, held that "[u]nder the peculiar circumstances of this particular case," (Cont'd)

Indeed, the Court has noted that it has reversed almost every finding of equitable estoppel on a government contract. *Office of Personnel Mgmt. v. Richmond*, 496 U.S. 414, 422 (1990).

In *Heckler*, the Court analyzed whether the government could be estopped from recovering funds erroneously paid to a medical care provider under the Medicare program, and concluded that it could not (i.e., that estoppel did *not* lie against the government). The medical care provider submitted cost reports (which were governed by regulation) which erroneously listed certain costs but which the government nevertheless paid because the regulations allowed for retroactive adjustments when the cost reports were periodically audited, should improper payments be made. Before submitting the cost reports, the medical care provider requested and received oral verification from the government's agent that the cost reports were, in fact, proper. However, when the government discovered the improperly paid costs, it sought to recover the money that was paid. The medical care provider attempted to assert that the government was estopped from recovering the money based upon the government's agent's oral verification. The Court held that estoppel was not proper because the regulations put the medical care provider on notice of the costs that were

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the government was estopped from bringing a lawsuit against the bank. Similarly, in *Resolution Trust Corp.* the court held that an estoppel affirmative defense in a lawsuit brought by Resolution Trust, a government agency, could survive a motion to strike by Resolution Trust, to the extent the estoppel affirmative defense was premised on some affirmative misconduct by the government. And, in *In re Lane*, the court noted that a government agency could not treat a contract as rejected after treating it as valid and after receiving the full benefit of the contract. None of these cases involved written loan documents or support a finding of estoppel in this case, where the government is not bringing suit, has not benefited and there is no claim of fraud or affirmative misconduct.

proper and because its reliance on an oral verification of policy by the government's agent was not reasonable.

In this case, as in *Heckler*, estoppel would not be proper. Here, West Pointe was on notice of the provisions of the Loan Documents and HUD regulations, which prohibit oral modifications of the loan documents and which state that only the Commissioner of HUD can authorize such modifications. In addition, the Trustee seeks not to estop the government based only upon a regulation, but also based upon a written loan document, which West Pointe signed. Thus, estoppel would not be proper because West Pointe had complete knowledge that the Loan Documents could only be modified with approval by the Commissioner.

In seeking to establish a basis for her claim of waiver, the Trustee once again seeks to create a dispute among the Circuits where there is none, this time erroneously analogizing the present action to the dispute at issue in *Spring Constr. Co. v. Harris*, 562 F.2d 933 (4th Cir. 1977). In *Spring Construction*, the court granted the plaintiff, a general contractor, relief against HUD for a ten percent retainage due from mortgage proceeds, holding that HUD had waived the defense of non-performance by continuing to encourage construction despite having knowledge of existing problems with the project. For many of the same reasons that the Trustee's reliance on *Pankow* as dispositive to the present action is incorrect, so too is the Trustee's reliance on *Spring Construction*.

The relationship from which the present dispute arises is between mortgage lender and borrower, a markedly different relationship than that of general contractor and mortgage lender, and indeed governed by different principles of legal responsibility and obligation. Furthermore, there is no evidence of HUD or CW "encouraging" West Pointe to

continue work on the Project such as to make claims of waiver relevant. Indeed, both the District Court and the Sixth Circuit found that the July 9, 1997 letter that the Trustee argues directs the parties to extend the contractual deadline indefinitely, "**plainly does the opposite**." Pet'r App. at A-10 (emphasis supplied).

Perhaps more important than this distinction, however, is the fact that the present action deals **specifically** with the alleged modification of HUD-insured loan agreements, while *Spring Construction* and other authorities relied upon by the Trustee[15] speak nothing to the modification of the rigidly governed terms of these HUD-prescribed loan instruments. Indeed, in *Spring Construction*, there was **no** modification of the terms of the building loan agreement or any other contract to which HUD was or was not a signatory. The central thrust of *Spring Construction* was whether non-completion of the contract was a sufficient defense for withholding mortgage retainage from the general contractor

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[15] Petitioner further relies upon the Federal Claims Court's ruling in *Carabetta Enters. Inc. v. United States*, 58 Fed. Cl. 563 (2003), as support for the assertion that acquiescence by conduct is sufficient to establish modification of the terms of a HUD-insured loan. In fact, however, the court in *Carabetta* found that HUD's offer of a capital loan (as opposed to the previously offered but subsequently repealed section 241(f) equity loans) and Carabetta's acceptance of such loan "**effected modification of the contract to that extent**." *Id.* at 567 (emphasis supplied). The court in no way extended this modification to the context of the overarching loan agreements governing issues of repayment and foreclosure such as are at issue in the present dispute. Indeed, the only reason such modification was granted was because of the clear acquiescence of both parties to accept the changed terms (clearly absent in the present dispute) and the fact that the subject loans originally agreed upon by the parties had been explicitly made illegal through Congressional action. The factual underpinnings of *Carabetta* are so distinct from the present action such that the court's holding in that case is clearly not dispositive of the present dispute.

such that claims for equitable relief by the general contractor would be unwarranted. *Spring Construction* speaks nothing to the underlying issue of the present action – the viability of non-written modifications (including theories of estoppel and waiver) to a HUD-insured loan agreement – and as such is clearly not a controlling authority in any manner.

D. Even If State Law Governed This Action, As Determined by the Lower Courts, Application of Tennessee Law Would Yield the Same Results.

The Trustee bases her Petition on the ground that the lower courts erred by applying federal law, which states that the doctrines of waiver and estoppel cannot modify the terms of a HUD-insured loan because federal regulations prohibit modification of a federally insured loan except through a written agreement. Pet'r App. at A-9. The Trustee argues that state law should apply and that, under state law, the result would be different. This is not the case.

First, the lower courts did analyze and reject the Trustee's claims under state law. *Id.* at A-11. Indeed, if (against the weight of authority) state law is applied, rather than federal law, the result is still the same. As the Sixth Circuit correctly noted in its decision, "West Pointe's waiver and estoppel claims are baseless even if we apply Tennessee common law." *Id.* at A-11.

The Tennessee Statute of Frauds states:

> No action shall be brought against a lender or creditor . . . upon any promise or commitment **to alter, amend, renew, extend or otherwise modify or supplement any written promise, agreement or commitment to lend money or extend credit**, unless the promise or agreement, upon which such action shall be brought, or some

> memorandum or note thereof, **shall be in writing** and signed by the lender or creditor, or some other person lawfully authorized by such lender or creditor.

Tenn. Code Ann. § 29-2-101(b)(1) (2003) (emphasis supplied). Moreover, under Tennessee law "all contracts, including . . . notes . . . shall be prima facie evidence that the contract contains the true intention of the parties and shall be enforced." Tenn. Code Ann. § 47-50-112(a) (2003). Thus, under Tennessee law, as under federal law, modification of a loan such as the loan at issue must be in writing. *See, e.g. Decatur County Bank v. Duck*, 969 S.W.2d 393 (Tenn. App. 1997) (affirming summary judgment in favor of lender on grounds that "absent writing memorializing" "alleged fraudulent representations by Bank that it would finance [borrower's] . . . operations until completion," such oral modification was unenforceable); *Bucholz v. Tenn. Farmers Life Reassurance*, 145 S.W.3d 80 (Tenn. Ct. App. 2003) (holding that modification of an existing contract cannot occur through an "ambiguous course of dealings" between the parties from which diverse inferences might reasonably be drawn as to whether the contract was modified or not); *Rush v. Chatanooga Du Pont Emp. Credit Union*, 210 Tenn. 344 (1962) (parol evidence is not admissible to vary, alter or contradict the terms of a written instrument); *Todd v. Third Nat'l Bank*, 172 Tenn. 586 (1938) (the terms of a note cannot be varied by oral proof and no legal conclusion can be rested upon statement of a bill which would vary positions of a note).

In addition, under Tennessee law, a waiver is an intentional relinquishment of a known right. *Ky. Nat'l Ins. Co. v. Gardner*, 6 S.W.3d 493, 498 (Tenn. 1999). To establish a waiver, "there must be a clear, unequivocal and decisive act of the party showing such a purpose or acts amounting to an estoppel on its part." *Id.* at 498-99. "The law will not

presume a waiver, and the party claiming the waiver has the burden of proving it by a preponderance of the evidence." *Id.* at 499. The Sixth Circuit found that West Pointe could not establish waiver. Pet'r App. at A-11-12.

Similarly, the Sixth Circuit rejected West Pointe's estoppel argument under Tennessee law. Estoppel, like waiver, "is not favored and it is the burden of the party seeking to invoke the doctrine to prove each and every element thereof." *Buchholz*, 145 S.W.3d at 85. The Sixth Circuit found that "West Pointe cite[d] no authority to suggest there is any jurisdiction that would find waiver or estoppel. . . ." Pet'r App. at A-12.

Under state law, as under federal law, West Pointe was unable to establish waiver and/or estoppel. Thus, any allegation that the lower court erred in applying federal law is moot, and not a basis for the grant of certiorari.

CONCLUSION

The Circuits are undivided in holding that mortgages administered under the National Housing Act cannot be modified by oral agreement, waiver or estoppel. Moreover, this is not a compelling federal issue which necessitates consideration by the Court. And, while federal law applies to loans administered under the National Housing Act, the results below would not differ under state law. Indeed, the lower courts correctly concluded that under the Tennessee Statute of Frauds, the HUD-Insured Loan could not be modified in any manner other than by a writing signed by the parties. For the foregoing reasons, CWCapital LLC respectfully requests that this Court deny the Petition.

Respectfully submitted,

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